

**BEAR STEARNS**

**RECEIVED**

**JUN 23 1997**

**ORIGINAL**

**FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY**

**BEAR, STEARNS & CO. INC.**

**245 PARK AVENUE  
NEW YORK, NEW YORK 10167  
(212) 272-2000  
FAX: (212) 272-3092**

**ATLANTA • BOSTON  
CHICAGO • DALLAS • LOS ANGELES  
NEW YORK • SAN FRANCISCO**

**SÃO PAULO • LONDON • PARIS • GENEVA  
BEIJING • HONG KONG • SHANGHAI • TOKYO**

**DOCKET FILE COPY ORIGINAL**

June 23, 1997

Mr. William F. Caton  
Acting Secretary  
Federal Communications Commission  
1919 M Street, N.W. Room 222  
Washington, D.C. 20554

Dear Mr. Caton:

This letter is in response to the Public Notice issued by the Federal Communications Commission ("FCC") on June 2, 1997 (WT Docket 97-82, DA 97-679). The Wireless Telecommunications Bureau ("Bureau") of the FCC has solicited comment on a number of issues relating to installment payments owed by broadband Personal Communications Services ("PCS") licensees. The Bureau seeks comments on several proposals that it has received and "invites any additional proposals for addressing the C and F block broadband PCS financing terms."

Bear, Stearns & Co. Inc. ("Bear Stearns") is a major investment bank involved in all aspects of securities underwriting, distribution and trading, as well as financial advisory services, for a wide range of corporate clients. Bear Stearns has been involved in the PCS industry since before the A- and B-block auctions. We assisted General Wireless, Inc. in raising a substantial amount of private equity capital prior to the conclusion of the C-block auction and attempted to raise public equity and high yield debt capital for several of the C-block licensees earlier this year.

I would like to address the C-block only, discuss why the C-block licensees are unable to raise additional funding in the current capital markets environment and set forth several alternatives available to the FCC to address this problem.

The essence of the C-block problem is that the value of the FCC obligation exceeds the value that equity investors are currently willing to assign to the entire company. A simple and imperfect analogy is a homeowner whose mortgage exceeds the market value of his house.

No. of Copies rec'd 084  
List A B C D E

To understand the issue it is important to consider two elements separately – the valuation of PCS companies and the value of the FCC obligation.

Fortunately, there are now several publicly-traded PCS companies. The values of these companies will be used by investors as benchmarks in valuing the C-block companies. The most relevant valuation parameter for comparing publicly-traded wireless telecommunications companies that are not generating earnings or cash flow is enterprise value per POP (i.e., person in the license area). Enterprise value measures the full value of the entire company, equity plus debt net of any cash available. To return to our house analogy, if one makes a \$20,000 down payment and obtains an \$80,000 mortgage to buy a house that happens to include a safe containing \$5,000 that stays with the house, the value of the house (the analogue of the enterprise value of a business) is \$95,000 – equity plus debt minus cash. In order to compare house values, one must know the value of each of these elements.

A comparison of the enterprise values of the four publicly-traded U.S. PCS companies is provided in Attachment A. The range of enterprise values per POP is \$28 to \$36. These companies have built networks and initiated service in at least some of their markets and are signing up subscribers and generating some level of revenues. They have spent \$4 to \$16 per POP on capital equipment alone since their inceptions and spent significant additional amounts on equipment installation as well as marketing and other costs associated with customer acquisition. Considering these advantages and the significant headstart enjoyed by their competitors, it would be wise to assume that the "average" C-block licensee would command an enterprise value that is a fraction (perhaps 30% to 40%) of the enterprise values of the publicly-traded PCS companies.

Each C-block licensee has a different amount of FCC obligation, but the analysis is similar for all of them. For simplicity we will deal with the "average" C-block licensee and analyze the issue on a "per POP" basis. The average net bid for a C-block license was \$40 per POP, using year-end 1990 POPs. Each licensee was required to make a 10% up-front payment (the average was \$4 per POP) and the FCC permitted deferred payment on 90% of the license cost, producing an average FCC obligation per POP of \$36.

The FCC designed the installment plan to be attractive to the designated entities. In particular, the coupon rate on the obligation is equal to the coupon on the most recent ten-year Treasury note at the time of license grant and the maturity is ten years with amortization commencing in the seventh year. In essence, the C-block licensees were allowed to borrow a substantial amount of money at terms available to the U.S. government. This is clearly well below the interest rate that a C-block company would have had to pay in the public market. Were the FCC to attempt to sell its obligation in the public market, it would realize proceeds substantially below the amount it is owed by the C-block licensees. In fact, the Securities and Exchange Commission and the accountants required the C-block licensees to record the value of the FCC obligation on their balance sheets at a substantial discount reflecting "prevailing rates for similar instruments of

issuers with similar credit ratings"<sup>1</sup>. Wall Street research analysts also favored reflecting a discount on the FCC obligation in assessing C-block valuations. The discount rate that seemed to be used most often by both the accountants and the Wall Street analysts in the period after the C-block auction was 14%. At a 14% discount rate, the present value of the FCC obligation is \$23 per POP on average, rather than the \$36 per POP average face value.

While the FCC provided substantial funding for the cost of the C-block licenses, the licensees still require significant funding for network buildout, operating losses and debt service. Equipment vendors have generally agreed to provide financing for equipment costs (and in some cases installation costs as well), but substantial funding requirements remain for debt service (particularly on the FCC obligation) and operating losses (largely the cost of acquiring subscribers prior to receipt of revenues from an existing subscriber base). The potential sources of this funding are public and private equity and high yield debt. Given the financing required, all but the smallest licensees are likely to require both debt and equity capital.

In order to raise this additional capital, it is necessary to demonstrate value. At current valuations, the value of the FCC obligations exceeds the enterprise value of the C-block licensees. Solving the C-block problem for the current licensees will require a substantial restructuring of the FCC obligation. The value of the FCC obligation must be reduced from its current average level of \$23 per POP to a level sufficiently below the enterprise value of the specific C-block licensee to provide adequate equity to support further debt and equity issues.

Several of the proposals made to the FCC to date address cash flow timing issues, seeking to better match the C-block licensees' cash requirements (interest and principal) with their projected cash receipts. Deferring cash requirements is very helpful to these licensees. Deferral can greatly reduce the amount of funding required as cash requirements that currently must be financed in the capital markets can be met from the licensee's internally-generated cash in future years. However, addressing the timing issue alone does not solve the fundamental C-block problem, which is valuation. In order for the C-block to raise substantial additional financing, either the market enterprise valuations of PCS companies must rise to levels closer to those that existed at the time of the C-block auction, or the FCC must restructure its C-block obligations in a way that dramatically reduces their value.

The two basic methods of restructuring the existing C-block obligations to lower their value are reduction or deferral of amounts owed -- principal and/or interest. As mentioned above, deferral alone is not likely to be sufficient. Attachment B sets forth several alternative combinations of interest and principal deferral and interest forgiveness and the resulting values of the FCC obligation. The substantial levels of value reduction required to attract additional C-block financing are only achieved through (1.) complete interest forgiveness and moderate deferral of principal or (2.) modest interest forgiveness and deferral combined with a substantial principal deferral.

---

<sup>1</sup> APB Opinion No. 21, Accounting Principal Board, paragraph 13.

There are several other modifications that the FCC can make to the terms of the C-block obligation or the C-block license rules that can be used to reduce substantially, in some cases, the impact of restructuring on the FCC's value. The most important of these is allowing the C-block licensees to prepay their FCC obligations at the restructured amount. In this way, the licenses (by far the most important tangible asset of the C-block licensees) are not subject to revocation for financial reasons. Junior, uncollateralized, lenders can then reasonably rely on the continuity of the business. Currently, potential junior lenders, such as high yield investors, must live under the threat that a financial stumble by the licensee leads to the revocation of the license and a full loss of value to the junior debt. A typical senior lender will have an interest in restoring the business to health working with its partners in the capital structure of the existing licensee.

In addition, prepayment would permit new senior lenders to collateralize their obligations with the licenses, at least indirectly, using the shares of the license-holding entity. This could greatly enhance the financial flexibility of the C-block licensees.

It is essential that prepayment be accompanied by a restructuring that is sufficient to create enough value to attract the substantial, though vastly reduced, capital required by the C-block licensees. However, by allowing the C-block licensees to prepay their FCC obligations, the FCC will greatly increase the benefit of any restructuring.

Consideration must be given to any C-block licensees whose FCC obligations are too large to prepay at one time. In order to make the prepayment option effective in these situations, the FCC must defer its payment obligations for a period of time sufficient to allow all prepayments to be made. This could be as long as two years in some circumstances.

In addition to prepayment, the FCC could consider any steps that make transferability of C-block licenses easier. The most meaningful of these steps would be the elimination of the requirement that any party not qualifying as a "designated entity" that acquires a C-block license between years five and ten of the license term must repay some portion of the original C-block bidding discount of 25%. This is viewed by investors as both an impediment to transfer and a limit on valuation. Of course, this modification would be unnecessary if prepayment were permitted.

Another modification that would enhance the financability of the C-block in a post-restructuring environment is an increase in the non-DE ownership limitation for a single investor above the current 25%. This improves the liquidity of the investment by allowing investors to take larger positions.

In summary, the critical element in addressing the C-block licensees' inability to finance in the current environment is to restructure the FCC obligation in a way that reduces its present value below the enterprise value associated with these companies, i.e., create equity value. The enterprise value associated with the C-block is substantially below that of the publicly-traded PCS companies, because these companies have spent hundreds of millions of dollars on their networks and established a considerable headstart in the wireless marketplace. Permitting prepayment will significantly enhance the ability to finance once an adequate restructuring is

Page 5  
Mr. William F. Caton  
June 23, 1997

accomplished. Additional modifications that facilitate transferability or improve investment liquidity would greatly improve the ability of the C-block licensees to raise the substantial funding they will still require.

Respectfully submitted,

Bear, Stearns & Co. Inc.

By: Norman C. Frost Jr.  
Norman C. Frost, Jr.  
Managing Director

PCS Public Company Market Valuation Comparison				
(In millions, except per POP Values)				
Ticker	<u>Omnipoint</u> OMPT	<u>Interce</u> ICEL	<u>Western</u> <u>Wireless</u> WWCA	<u>Aerial</u> <u>Comm</u> AERL
Share Price on 6/19/97	\$15.00	\$13.63	\$12.63	\$8.63
Fully Diluted Shares Outstanding	58.7	36.0	75.8	71.5
Equity Value	\$880.4	\$489.9	\$956.7	\$616.6
Govt. Debt	771.2	0.0	0.0	0.0
Adj. to Govt. Debt	(95.8)	0.0	0.0	0.0
<u>Other Debt</u>	536.5	551.4	1,138.7	188.3
Plus Total Debt	1,211.9	551.4	1,138.7	188.3
Balance Sheet Cash	(199.9)	(259.7)	(53.1)	(7.1)
Options and Warrants Cash	(43.2)	0.0	(40.2)	0.0
Less Total Cash	(243.1)	(259.7)	(93.3)	(7.1)
Less Minority Interest	0.0	(2.6)	0.0	0.0
Less Non-PCS Assets	(100.0)	(47.7)	(1,101.3)	0.0
<b>PCS Enterprise Value</b>	<b>1,749.2</b>	<b>731.3</b>	<b>900.8</b>	<b>797.8</b>
Adjusted 1995 PCS POPs				
30 MHz @ 100%	39.1	17.3	19.4	27.4
3 10MHz Licenses @ 100%	0.1	0.0	0.0	0.0
2 10 MHz Licenses @ 75%	12.7	0.0	0.3	0.0
1 10 MHz License @ 25%	<u>9.7</u>	<u>3.1</u>	<u>12.2</u>	<u>0.0</u>
Total	61.7	20.3	31.8	27.4
<b>PCS License Value / Adjusted POP</b>	<b>\$28.37</b>	<b>\$35.97</b>	<b>\$28.33</b>	<b>\$29.08</b>

**Federal Communications Commission**  
**C-Block Debt Restructuring Alternatives<sup>(1)</sup>**

<b>Status Quo Principal Amortization</b>				
<b>Status Quo</b>	<b>5 Yr. No Interest &amp; 5 Yr. Cash Pay</b>	<b>5 Yr. Interest Accrual &amp; 5 Yr. Cash Pay</b>	<b>10 Yr. Interest Accrual</b>	<b>10 Yr. No Interest</b>
<b>\$23.10</b>	<b>\$14.78</b>	<b>\$20.41</b>	<b>NM</b>	<b>\$11.92</b>
64.2%	41.1%	56.7%	NM	33.1%
<b>Principal Deferral Scenarios</b>				
<i>All Principal Repaid in Year 10</i>				
<b>Status Quo</b>	<b>5 Yr. No Interest &amp; 5 Yr. Cash Pay</b>	<b>5 Yr. Interest Accrual &amp; 5 Yr. Cash Pay</b>	<b>10 Yr. Interest Accrual</b>	<b>10 Yr. No Interest</b>
<b>\$23.10</b>	<b>\$13.27</b>	<b>\$18.32</b>	<b>\$17.33</b>	<b>\$9.09</b>
64.2%	36.9%	50.9%	48.1%	25.3%
<i>All Principal Repaid in Year 15</i>				
<b>Status Quo</b>	<b>5 Yr. No Interest &amp; 10 Yr. Cash Pay</b>	<b>5 Yr. Interest Accrual &amp; 10 Yr. Cash Pay</b>	<b>15 Yr. Interest Accrual</b>	<b>15 Yr. No Interest</b>
<b>\$23.10</b>	<b>\$10.85</b>	<b>\$14.98</b>	<b>\$12.02</b>	<b>\$4.57</b>
64.2%	30.1%	41.6%	33.4%	12.7%
<i>All Principal Repaid in Year 20</i>				
<b>Status Quo</b>	<b>5 Yr. No Interest &amp; 15 Yr. Cash Pay</b>	<b>5 Yr. Interest Accrual &amp; 15 Yr. Cash Pay</b>	<b>20 Yr. Interest Accrual</b>	<b>20 Yr. No Interest</b>
<b>\$23.10</b>	<b>\$9.63</b>	<b>\$13.30</b>	<b>\$8.34</b>	<b>\$2.30</b>
64.2%	26.8%	36.9%	23.2%	6.4%

(1) All analysis assumes a \$40 per 1990 POP average license cost and FCC financing @ 90% of license cost. Percentages represent market value of FCC financing as a percent of the face value, assuming quarterly interest (@ 6.5%) and principal payments and a 14% discount rate.